Overview of Risks & Internal Controls for NGOs

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Why understand risk management

- Risks is a must discussion now in NGO-funder relationship, idea is how to understand, capture and manage risks by NGOS.
- Good risk management is (a) basic to an effective organisation and (b) ensures better delivery of services to community.
- Fundamental concepts in organisation risk management- risk appetite (willingness to take risk to achieve objectives) and risk tolerance (ability or boundary to take risk/acceptable deviation from risk appetite). Risk appetite is about "taking risk" and risk tolerance is about "controlling risk".
- Risk appetite denoted risk profile at aggregate level while risk tolerance is at activity level i.e. on case by case basis.
- Risk management is how to bridge the gap between risk appetite and tolerance.
- Understand the need for internal controls commensurate with risks.

Why risk management is important for NGOs

1. Financial stability
2. Operational Efficiency
3. Compliance Management
4. Disciplined Planning
5. Informed decision making
6. Reputation Management
7. Building Trust
8. Improved communication
9. Long term Impact and Sustainability

Key concepts

- **Threat**: A danger in the environment, a potential cause of harm. e.g. legislative changes, technology, competition, inflation, globalisation etc.
- **Risk**: The probability and potential impact on achievement of objectives while encountering a threat.
- **Internal risks**: personnel issues, technology issues etc within the organization.
- **External risks**: economic, political, legal, act of God etc. in external environment.
- **Residual risk**: The risk which inevitably remains after all reasonable mitigation measures have been taken.
- No organization is completely free from risks. The environment will always contain risks.
- **Risk management/mitigation**: Organizational practices, procedures and policies (P&Ps) that reduce the probability of risks being realized and limit harmful consequences.
- **Enterprise/Integrated risk Management (ERM)**: An organizational management that considers, combines, and prioritizes assessed risks in all risk areas (security, fiduciary, operational, informational, and reputational) in order to strategize and implement mitigation measures.
- Risk mitigation is risk reduction, it cannot be made zero.

Types of risks facing Organisations

- Ethical risk: due to unethical behaviour

- Operational risk: inability to achieve objectives, capacity/competence gaps, financial/funding constraints, access constraints
- Safety risk: accident/illness
- Financial risk: improper financial planning and management
- Reputational risk: damage to image and reputation
- Security risk: violence/crime
- Fiduciary risk: breach of trust like corruption/fraud/theft/diversion
- Legal/compliance risk: violating laws or regulations
- Information risk: data breach/loss, digital risk, systems breach
- Competition risk: competitor take your market for goods/services

Risk Management Policy- Need

- Donor audits/due diligence by prospective donors
- Need to instil a sense of identifying, understanding and addressing risks in the organisation as it grows
- Create awareness about risk mitigation strategies when faced with risks in our respective areas of work.
- Staff embrace and own risk management process
- Act as a tool for governance and control

Risk Management Process

1. Risk universe analysis
2. Risk identification
3. Risk assessment-risk assessment matrix based on likelihood and impact of identified risks

Risk Management Process

- Prioritise risks to be taken up for mitigation
- Risk Response-Risk Registers with Roles and responsibilities of staff
- Monitoring

- Reporting

Internal Controls

- Business practices that serve as "checks and balances" on internal stakeholders (staff/key functionaries) and/or external stakeholders (vendors) in order to reduce the risk.
- Internal controls are mechanisms or procedures or rules to mitigate or reduce the risks and loss to an acceptable level.
- Internal Controls are of 3 types-
  a. preventive controls: in place to prevent adverse events
  b. detective controls: detect error/problem after it has occurred-internal audits, Reconciliations, physical inventorying
  c. Corrective controls-based on error detected

Benefits and Limitations of Internal Controls

Benefits

- Early warning system
- Prevents fraud
- Avoids external audit findings
- Avoids statutory and regulatory penalties and actions
  Limitations

1. Collision
2. Human error
3. Unforeseen circumstances

Key Areas of Internal Controls in NGOs

- The below Internal Controls can be grouped into one of the following buckets:
  (a) Financial Controls

(b) Operational Controls

(c) Compliance Controls

- The below are illustrative but not exhaustive and discussed in following slides:
  - Legal compliance
  - Governance
  - Budget
  - Income
  - Expenditure
  - Purchase/Procurement
  - Human Resource Management
  - Assets/Inventory Management
  - Accounting
  - Cash and Bank
  - Donor Reporting
  - Program Implementation

1. Internal Controls around Legal compliance

- Statutory and regulatory compliance-difference
- All applicable statutory registrations are in order and valid (entity registration, 12AB, 80G, PAN, TAN, FCRA, NGO Darpan, MCA, EPF, ESIC, PT, Shops & Establishments Act etc).
- All annual/periodic regulatory filings upto date (ITR, TDS, EPF, ESI, PT ROS/ROC etc).
- Proactively check adverse proceedings/pending matters under various laws.
- Aware that a statute or rule applies to NPOS.
- Continued education/awareness/knowledge for changes happening in statutory and regulatory landscape.

2. Internal Controls around Governance

- Board has fiduciary (manage assets/resources for someone) duties/responsibilities.
- Governance structure as per bye laws/rules.
- Meetings as per bye laws, proceedings documented as minutes of meeting.
- Changes notified & approvals obtained from statutory bodies.

- Board to put in place risk management/mitigation system.
- All statutory and other business as per timeline after proper scrutiny and review.
- Legal action against/violations by board members.
- Section 13 disallowances for transactions with board members.
- Approval of P&Ps and sub committees.

3. Internal controls around Budgeting & Budgetary Controls

- What is a budget?
- How budget helps organisation in planning and execution of grant projects.
- What is Budgetary Controls-process, periodicity, ownership of program and finance teams.
- Course correction/Budget revision to address deviation/variance (favorable or adverse).

4. Internal controls around Grants and other Incomes

- Grant funds credited in designated Bank account.
- Grant-proper safety and record keeping.
- Treatment of interest.
- Periodic grant Reconciliation.
- Segregation of duties in Finance.
- issuance of money Receipt and donation certificate to donor.
- Timely reporting.
- Proper receipt and recording of income other than grants which include rent, interest, incidental business activity etc.

5. Expenditure

- Programme Expenditure or Administrative Expenditure
- Revenue or Capital Expenditure
- Head Office Expenditure or Field Level Expenditure

Internal Controls around Expenditure

- Expenditure plan aligned with field requirement and project plan.
- Monitoring to prevent misappropriation/excessive spend/fraud.
- Qualified Finance Staff to avoid inaccurate/delay in payments.
- Proper recording of transactions, report and invoices.
- Tracking over-utilisation and under-utilisation of expenses under budget head for donor budgets for reallocation/realignment.
- Proper filing/documentation (bills, vouchers, invoices).

6. Internal Controls around Purchase/Procurement

- Procurement is act of buying or obtaining goods/services. It includes preparation and processing of a demand until the end receipt is obtained and payment is approved and released.
- Procurement process cycle.

Internal Controls around Purchase/Procurement

- Initiate procurement after checking budget provision.
- Identify vendors after proper assessment.
- Vendor database.
- Obtaining appropriate bids/tenders.
- Competitive bids for price discovery.
- Proper scrutiny of bids by the PC.
- Terms and conditions in PO/contract.
- Issue of Purchase Orders (PO) by authorized staff only.
- Accurate and complete information in the PO.
- Procurement tracker.

7. Human Resource (HR) Management

- Management of people who work in an organization is HR Management.
- Need to manage HR:
    - For better management of an organization.

    - For better performance and results.
    - For better resource mobilization and funding for the organization.

Controls around HR Management

- HR Planning
- Recruitment of staff as per JD
- Proper orientation for new recruits
- Avoid Nepotism
- Identification of capacity building needs and training of HR
- Objective performance appraisal
- Proper handing over for exiting employee
- Discontinue access to database for resigned employee
- Maintaining Employee personal information
- Salary structure
- Grievance and complaints redressal mechanism
- Compliance with social security laws for employees

8. Fixed Assets & Inventory Management

- FA is item of economic value which has a life of more than 1 year.
- Inventory refers to items such as consumables, durables that are normally consumed within a year.

Controls around Fixed Assets & Inventory

- Asset & Inventory management section in finance policy.
- Indent for assets and consumables based on need and budget.
- Purchase approved by PC and as per grant budgets.
- Specification of assets/inventory captured in PO.
- Annual verification of fixed assets and consumables.
- FA Register, Asset Identification No. marking on assets.
- Assets which are disposed off are removed from FA Register.
- Stock Register of consumables.

- Sale of FC assets.
- Disposal of building, land or higher value assets after Board approval and treatment of CG.

9. Internal Controls around Accounting

- Accounting is the process of recording, summarizing, analyzing and reporting financial transactions.
- Area of internal control in accounting-
  - Compliance with new Rule regarding maintenance of books of accounts.
  - Compliance with new Rule regarding maintenance of Other documents.
  - Accounting Software Controls in accounting:
    - Accuracy
    - Standard formats for recording
    - Evidence and supportings
    - Complete and transparent
    - Audit

10. Controls around Cash and Bank transactions

- Cash is kept in cash box (fixed to wall).
- Reduce cash transaction and practice online options/universal banking.
- Cash vouchers numbered and Receipts duly signed by receiver and approved.
- Dual signatory.
- Monthly bank reconciliation.
- Control on cash withdrawal transactions.
- Signatories per delegation.
- Update KYC of signatories.
- Promote online banking.

11. Controls around Donor compliances

- Timely and accurate preparation of reports.
- Activities are in line with activity schedule.
- Data properly collected with reference to objectives of program.
- Donor reporting guideline and formats are adhered to.

12. Controls around Program Implementation

- Project Implementation plan carried out as per proposal.
- No/ minimal mismatch between LFA and budget.
- Impact of adverse events are effectively monitored.
- Program implementation is effectively monitored in audit.
- Appropriate tools of assessment are used.
- Data presentation is properly done.
- Outcome of program is properly reported.

Concept of Efficiency & Effectiveness

- In non profits, efficiency refers to maximizing impact with available resources, while effectiveness assesses whether the NGO achieves its stated goals and outcomes.
- Efficiency focuses on how resources are used while effectiveness focuses on the results achieved.
- Efficiency measures the degree to which an organization can convert inputs (funds, time, manpower) into intended outputs (programs, services, people served).
- It emphasizes minimizing waste and maximizing value for each unit of resource invested.

- Effectiveness assesses whether an NGO is achieving its stated goals and objectives, and whether it's making a significant difference in its area of operation.
- It assesses outcomes and impact, including whether lives are being improved and problems are being solved.
- Examples: Tracking progress toward goals, measuring outcomes, and evaluating long-term impacts are ways to assess effectiveness.

	Efficiency	**Effectiveness**
Definition	Efficiency refers to the act of performing activities with minimum wastage of time and optimum usage of resources timely and without error.	Effectiveness is the extent to which someone or something is successful towards meeting the desired outcome.
Focuses on	Doing the assigned task in a correct way	Doing the assigned task accurately
Focuses on	Efficiency is focused on the inputs and outputs	Effectiveness is focused on the extent to which work is done and the end result achieved
Effort oriented	Efficiency is effort oriented on operations	Effectiveness is effort oriented on strategy
Time oriented	Efficiency is time oriented	Effectiveness is not time oriented

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